

ORIGINAL

**COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION
AT RICHMOND**

At the relation of the

CASE NO. PUE-2002-00645

STATE CORPORATION COMMISSION

**Ex Parte: In the matter concerning
the provision of default service to retail
customers under the provisions of the
Virginia Electric Utility Restructuring Act**

Statement of Interest and

Comments of Reliant Resources, Inc. on the Provision of Default Service

Reliant Resources, Inc. ("Reliant") appreciates the opportunity to comment on the questions posed by the State Corporation Commission related to default service. Reliant is one of the largest merchant generators in the United States, with 16,000 MW of operational capacity of which 7,500 MW is located in the mid-Atlantic area of the United States. Reliant's retail group offers a full suite of commodity, energy management and other energy related services to large users of electricity. Reliant is interested in participating in promising retail markets as they evolve as part of its business strategy.

Reliant offers a unique perspective having served as Default Provider and Provider of Last Resort ("POLR") in several jurisdictions. Reliant currently delivers wholesale supply used in Duquesne Light's POLR Service. In addition, Reliant won a bidding process to be POLR to all large industrial customers within Texas and to residential and commercial customers for most of the area outside Reliant's traditional utility service territory. Drawing on lessons learned through its experience as a default provider and POLR in other jurisdictions, Reliant respectfully offers its comments regarding what it believes should be the key features of appropriately designed Default and POLR service.

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Types of Default Service

The umbrella term default service, as used in the Virginia statute,¹ includes three distinct considerations:

- 1) Default service to customers who do not select a competitive retail provider;
- 2) POLR service for customers whose retail provider fails to provide service as in the case of a retail provider bankruptcy; and
- 3) Policies for payment-challenged customers.

We advocate NOT using the terms default service and POLR service interchangeably. Default service is a short-term market design element in the transition to competition, whereas POLR service is likely to be a permanent market design element for residential and small commercial customers. POLR service should be a stopgap service until the customer can switch to a competitive supplier. The POLR service provider faces greater risks than default or competitive service due to the highly unpredictable load.

Price

The cornerstone to successful design of both Default and POLR service is to have prices linked in some manner to changes in the wholesale market price of electricity. The presence of a Default/POLR service price introduces a *de facto* cap on retail prices. In general, customers will not change suppliers if they must pay a higher price. Therefore, competitive retail providers must be able to offer prices lower than the Default and POLR service prices. Moreover, competitive retail providers need certainty that as market prices change, the Default and POLR service prices will adjust such that competitive retail providers are able to offer prices lower than the Default and POLR service prices over time. However, competitive providers will not enter the market unless they can offer the lower price and still profitably cover the cost of acquiring and serving customers. Therefore, initial headroom between the benchmark prices of Default and POLR services and the wholesale market price is also required.

¹ Virginia Electric Utility Restructuring Act, § 56-576, *et seq.* of Title 56 of the Code of Virginia.

Phase-in

It may be appropriate to differentiate Default and POLR service designs for residential and small commercial customers versus large commercial and industrial customers, and to phase-in the different designs at a different pace.

Selection of Default and POLR Provider

RRI supports market-oriented solutions to the provision of Default and POLR providers. For Default service, the incumbent utility may transfer customers who do not choose another provider to a competitive affiliate; or if the utility prefers, allow providers to bid to provide Default service. The POLR service provider should be selected by competitive bids.

RRI Responses to Questions

(1) What should be the specific components of default service?

(A) The umbrella term default service, as used in the Virginia statute, includes three distinct considerations:

- (1) Service to customers who do not select a competitive provider;
- (2) POLR service for customers whose provider fails to provide service such as a provider bankruptcy; and
- (3) Policies for payment-challenged customers.

All three encompass much of what is traditionally utility service, *e.g.* capacity, energy, transmission, distribution, ancillaries, billing, customer service and metering.²

(2) Whether, given the virtual absence of competition in Virginia's retail generation market, incumbent electric utilities should continue to provide default service at capped rates at the present time; if so, what changes in statute, policy, infrastructure, market conditions, and/or other circumstances

² Transmission and distribution would be provided by the utility to the Default/POLR provider.

are necessary to allow for the practical provision of default service by an entity other than the incumbent?

- (A) The absence of competition in Virginia is driven by two main factors. First, incumbent rates are capped at a level below which a competitive provider can enter the market. Second, the fact that incumbent utilities in Virginia will evidently not become members of a Regional Transmission Organization ("RTO") prior to 2004.

Changes needed include:

- (i) Joining an RTO. We understand that, pursuant to recent legislation, this is unlikely to occur prior to 2004. Joining an RTO provides market participants increased certainty of independence of the operation of the transmission system and the operational market for ancillary and energy services and settlements.
- (ii) Linking Default and POLR prices to market prices. To the extent that the incumbent utilities offer Default and POLR service, this link will be difficult to achieve prior to the end of the rate cap period(s).
- (iii) Headroom between Default and POLR prices and wholesale prices. Again this will be difficult to achieve prior to the end of the rate cap period(s).

What should be the geographic scope of a default service provider's territory, i.e. statewide, incumbent utility service territory, regions served by specific regional transmission entities; divisions with an incumbent utility's service territory; major metropolitan and surrounding areas, etc.;

- (B) Given historical boundaries for rate design and price differences under regulation, Default and POLR service territories should be the same as incumbent utility service territory.

- (3) **Whether default service, as contemplated by §56-585 of the Act, should be limited to unregulated services, i.e. is it necessary to designate distribution service as a default service:**

(A) Where feasible, Default and POLR services should be provided directly to the customer and encompass all necessary services.

(4) For generation-related default service, whether the separate components of generation service to retail customers (capacity or resource reservation, energy, transmission, and ancillary services) should be treated as separate default services or bundled into a single service.

(A) Default and POLR services should each be a single service; however the components may be unbundled on the customer's bill.

(5) For generation-related default service, whether the service should be delivered to the retail customer or to the incumbent utility;

(A) Where feasible, Default and POLR services should be delivered to the retail customer. The model of delivering default service to the incumbent utility is currently being tested in New Jersey under the BGS Auction design. While we appreciate this as one model for default service, the ultimate goal should be the delivery of default service as a retail service.

(6) Whether the language of the statute prohibits the provision of default service to an incumbent utility on behalf of a group of customers, i.e. could a third party provide service to an incumbent utility for indirect service to retail customers (service to satisfy load growth, specific localities, or to customer subgroups);

(A) Reliant has not formed an opinion on the statutory provisions related to the service identified in the question. However, these services do not comport with the definition of Default or POLR service.

(7) Whether the provision of default services should differ by customer class;

(A) Residential and small commercial customer Default and POLR service pricing should be linked to long-term (not spot), forward looking wholesale market

prices. Large customer POLR³ service pricing should be linked to spot wholesale market prices.

(8) Whether different components of default service can be provided by different suppliers;

(A) Different suppliers could supply Default and POLR service to different classes of customers, or to different service areas.

(9) Whether default service has the same meaning for different classes of customers, i.e, those who do not affirmatively select a supplier, those who are unable to obtain service from an alternative supplier, or those who have contracted with an alternative supplier who fails to perform;

(A) The umbrella term default service, as used in the Virginia statute, includes three distinct considerations:

- 1) Service to customers who do not select a competitive provider;
- 2) POLR service for customers whose provider fails to provide service such as a provider bankruptcy; and
- 3) Policies for payment-challenged customers.

The framework for pricing and terms and conditions should consider the different risks associated with each of the different types of service.

(10) How should charges for default service be collected;

(A) Eventually, each Default and POLR provider should bill and collect remittances from customers. It may be appropriate, for a transition period, for the incumbent utility to perform billing and collection.

(11) Whether metering, billing and collecting services should be deemed components of default service;

(A) Metering, billing and collecting services should eventually be provided by the Default and POLR service providers. If the provider is not the incumbent

³ No Default service, as defined by Reliant, is necessary for large industrial customers.

provider it may be desirable to have a transition period where these functions are provided by the incumbent.

(12) What implications would the alternative provision of default service have for the determination of wires charges?

(A) None identified.

Communications

Please add the following persons to the service list in this proceeding.

Michael G. Briggs
Senior Counsel
801 Pennsylvania Avenue, NW
Suite 620
Washington, D.C. 20004-2604
Telephone: (202) 783-7220
Facsimile: (202) 783-8127
E-mail: Mbriggs@reliant.com

Martha Duggan
Regional Manager, Regulatory Affairs
Reliant Resources, Inc.
3102 North 6th Street
Arlington, Virginia 22201
Telephone: (703) 312-0960
Facsimile: (703) 312-0235
E-mail: Mduggan@reliant.com

RESPECTFULLY SUBMITTED


Michael G. Briggs

Counsel for Reliant Resources, Inc.

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